

## **Initial Statement of Reasons**

### **Adoption of Proposed Amendments to California Code of Regulations, Title 18, Sections 4601, *Service of a Notice of Violation or Warning Notice*, 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers***

#### **SPECIFIC PURPOSE AND NECESSITY**

##### Current Law

On October 12, 2003, the State of California enacted Assembly Bill No. (AB) 71 (Stats. 2003, ch. 890 (Horton)), and section 1 of AB 71 added the Cigarette and Tobacco Products Licensing Act (Act) to division 8.6 (commencing with section 22970) of the Business and Professions Code (BPC). As originally enacted, the Act imposed licensing requirements on all retailers, wholesalers, and distributors of cigarettes and tobacco products and all manufacturers and importers of cigarettes. In 2006, the State of California enacted AB 1749 (Stats. 2006, ch. 501 (Horton)), which added new provisions to the Act that imposed the same licensing requirements on manufacturers and importers of tobacco products as were previously imposed on manufacturers and importers of cigarettes.

The Act is administered by the State Board of Equalization (Board) pursuant to BPC section 22971.2, and, in 2006, the Board adopted a number of regulations to implement, interpret, and make specific the Act's licensing requirements. As relevant here, the Board adopted California Code of Regulations, title 18, sections (Regulations) 4600, *Issuance and Contents of a Notice of Violation or Warning Notice*, and 4601, *Service of a Notice of Violation or Warning Notice*, to require the Board to issue a Notice of Violation or Warning Notice to and serve such notice on a person that has been issued a citation for a violation of the Act. Regulation 4601 currently provides that:

The Notice of Violation or Warning Notice shall be placed in a sealed envelope, with postage paid, addressed to the licensee or unlicensed person at his or her last known address as it appears in the records of the Board. The giving of notice shall be deemed complete at the time of deposit of the notice at a United States Post Office, a mailbox, sub-post office, substation, mail chute, or other facility regularly maintained or provided by the United States Postal Service, without extension of time for any reason. In lieu of mailing, a Notice of Violation may be served personally by delivery to the person to be served and service shall be

deemed complete at the time of such delivery. Personal delivery to a corporation may be made by delivery of a notice to any person designated to be served for the corporation with summons and complaint in a civil action, pursuant to the Code of Civil Procedure.

The text of Regulation 4601 is based upon the text of Revenue and Taxation Code (RTC) section 30206, which provides for the service of a notice of determination issued under the Cigarette and Tobacco Products Tax Law (RTC § 30001 et seq.).

The Board also adopted Regulations 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed and Unlicensed Manufacturers and Importers*, to provide for the issuance of a Warning Notice, or the imposition of a 10-day, 20-day, or 30-day suspension, or the revocation of a license and the imposition of a fine for specified violations of the Act; and to provide for the reduction in the length of a suspension and changing a revocation to a 30-day suspension, when mitigating factors warrant. As relevant here, the second and third sentences in subdivision (f) of Regulations 4603 and 4604 and subdivision (e) of Regulation 4605 all currently provide that:

If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.4, 22978.6, or 22980.3, subdivision (a)(2).

#### Specific Purpose, Necessity, and Benefits of the Proposed Amendments

##### *Amendments to Regulation 4601*

A person has the right to appeal when the Board has alleged that the person violated the Act. When timely appeals are made, the Board is required to issue notices under Regulations 4700, *Appeal – Special Taxes and Fees Division*, 4701, *Appeal – Appeals Division*, and 4702, *Appeal – Board Hearing*. However, Regulation 4601 only prescribes the manner of serving a Notice of Violation or Warning Notice, and there is no regulation expressly prescribing the manner in which the Board shall serve other notices required to be served under the Act, such as the notices required by Regulations 4700 through 4702. Therefore, to specifically address the problem, Board staff prepared Formal Issue Paper 12-007, which recommended that the Board

1. Amend Regulation 4601 so that it applies to all of the notices the Board is required to serve under the Act and requires that all of the notices be served in the manner provided for in RTC section 30206 for the service of a notice of determination; and
2. Shorten the name of Regulation 4601 to “Service of a Notice” to reflect the expanded application of the regulation’s provisions.

The Board considered Formal Issue Paper 12-007 during its Business Taxes Committee meeting on June 26, 2012. The Board agreed with staff's recommendations and unanimously voted to propose the adoption of staff's recommended amendments to Regulation 4601 because the Board determined that the amendments were reasonably necessary to expressly prescribe the manner in which the Board shall serve all the notices required to be served under the Act and make the name of Regulation 4601 consistent with its amended contents.

The text of the proposed amendments to Regulation 4601 is slightly different than the text of staff's recommended amendments to Regulation 4601, as shown in exhibit 3 to Formal Issue Paper 12-007. The text shown in exhibit 3 to the issue paper provided that "Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice of determination under Revenue and Taxation Code section 30206 of the Cigarette and Tobacco Products Tax Law." However, section 22971.5 was added to the BPC after the Board's adoption of Regulation 4601 to prescribe the manner for serving any notice required under the Act. Therefore, the Board revised staff's recommended amendments to Regulation 4601, prior to beginning the formal rulemaking process, in order to make the text of the Board's proposed amendments to Regulation 4601 fully consistent with the provisions of BPC section 22971.5, which are substantially similar to the provisions of RTC section 30206. The Board's proposed amendments provide that "Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice under Business and Professions Code section 22971.5." In addition, the Board has proposed to amend Regulation 4601's reference note so that it only refers to BPC section 22971.5.

The Board has determined that the proposed amendments to Regulation 4601 are reasonably necessary to expressly prescribe the manner in which the Board shall serve all the notices required to be served under the Act and make the name of Regulation 4601 and the regulation's reference note consistent with the regulation's amended contents. The Board also determined that the proposed amendments to Regulation 4601 are reasonably necessary to specifically address the problem created by the regulation's lack of guidance regarding the service of notices, other than Warning Notices and Notices of Violation, that the Board is required to serve under the Act, and the Board anticipates that the public, including regulated persons, will benefit from the increased openness and transparency regarding the procedures for the service of all notices required under the Act.

#### *Amendments to Regulations 4603 through 4605*

Regulations 4603 through 4605 provide that a suspension period may be reduced to "0 days, 10 days, or 20 days" when mitigating factors warrant, but the regulations do not give the Board sufficient flexibility to reduce suspensions because there are situations where a 10-day suspension is too harsh, a 0-day suspension would not be sufficient to deter violations of the Act, and a suspension period of more than 0 days and less than 10

days would be appropriate. Therefore, Board staff initially recommended that the Board amend Regulations 4603 and 4605 to provide for the reduction of a suspension within a range of between 1 and 20 days to give the Board more flexibility. However, some interested parties objected to staff's initial recommendation because they felt that shorter suspension periods, such as 1 day, would not be sufficient to deter violations of the Act and would be difficult for the Board to enforce.

As a result, Board staff alternatively recommended that the Board amend Regulations 4603 through 4605 to provide for the reduction of a suspension to "5 days," in addition to 0 days, 10 days, and 20 days. The alternative recommendation was based upon staff's belief that a 5-day suspension period is long enough to deter violations of the Act, in some circumstances, and that Board staff has a sufficient amount of time to perform an inspection during a 5-day suspension period.

Board staff presented both of its alternative amendments to Regulations 4603 through 4605 to the Board as part of Formal Issue Paper 12-007. Mr. Steven Alari, representing SEIU Local 1000, appeared at the Board's June 26, 2012, Business Taxes Committee meeting and generally supported staff's recommendation adding a 5-day suspension period to all three regulations. As a result, the Board unanimously voted to propose adding a 5-day suspension period to the regulations because the Board determined that the amendments were reasonably necessary to specifically give the Board additional flexibility to reduce suspensions. The Board also determined that the amendments to Regulations 4603 through 4605 are necessary to address the problem that currently exists when a 10-day suspension is too harsh, a 0-day suspension would not be sufficient to deter violations of the Act, and a suspension period of 5 days would be more appropriate, and the Board anticipates that the Board and regulated persons will benefit by the establishment of a fair, 5-day suspension period to address such situations.

In addition, Regulation 4603 applies to retailers, and subdivision (f) of Regulation 4603 provides that a retailer's revocation penalty will not be reduced to a 30-day suspension if revocation is required by specified BPC sections, including BPC section 22978.6. However, section 22978.6 provides for the revocation of distributors' and wholesalers' licenses, not retailers' licenses. Also, subdivision (f) of Regulation 4603 does not refer to BPC sections 22974.3, subdivisions (a)(2) and (a)(4), and 22980.3, subdivision (d), and these subdivisions do require the revocation of retailers' licenses for specified violations of the Act. Therefore, in Formal Issue Paper 12-007, Board staff recommended deleting the reference to BPC section 22978.6 from subdivision (f) of Regulation 4603, adding references to BPC sections 22974.3, subdivisions (a)(2) and (a)(4), and 22980.3, subdivision (d), to subdivision (f) of Regulation 4603, and adding a reference to BPC section 22980.3, subdivision (d), to Regulation 4603's reference note.

Further, Regulation 4604 applies to wholesalers and distributors, and subdivision (f) of Regulation 4604 provides that a wholesaler's or distributor's revocation penalty will not be reduced to a 30-day suspension if revocation is required by specified BPC sections, including BPC section 22974.4. However, section 22974.4 provides for the revocation of retailers' licenses, not wholesalers' and distributors' licenses. Also, subdivision (f) of

Regulation 4604 does not refer to BPC sections 22978.2, subdivisions (a)(2) and (a)(4), and 22980.3, subdivision (d), and these subdivisions do require the revocation of wholesalers' and distributors' licenses for specified violations of the Act. Therefore, in Formal Issue Paper 12-007, Board staff recommended deleting the references to BPC section 22974.4 from subdivision (f) of Regulation 4604 and Regulation 4064's reference note, adding references to BPC sections 22978.2, subdivisions (a)(2) and (a)(4), and 22980.3, subdivision (d), to subdivision (f) of Regulation 4604, and adding a reference to BPC section 22980.3, subdivisions (a)(2) and (d), to Regulation 4604's reference note. Board staff also recommended moving the reference to BPC section 22978.7 in Regulation 4604's reference note so that all of the statutory references in the reference note are in numerical order.

Furthermore, Regulation 4605 applies to manufacturers and importers, and subdivision (e) of Regulation 4605 provides that a manufacturer's or importer's revocation penalty will not be reduced to a 30-day suspension if revocation is required by specified BPC sections, including BPC sections 22974.4 and 22978.6. However, BPC sections 22974.4 and 22978.6 do not apply to the revocation of manufacturers' and importers' licenses. Also, subdivision (e) of Regulation 4605 does not refer to BPC section 22980.3, subdivision (d), and this subdivision does require the revocation of manufacturers' and importers' licenses for a specified violation of the Act. Therefore, in Formal Issue Paper 12-007, Board staff recommended deleting the references to BPC sections 22974.4 and 22978.6 from subdivision (e) of Regulation 4605, adding a reference to BPC section 22980.3, subdivision (d), to subdivision (e) of Regulation 4605, and adding a reference to BPC section 22980.3, subdivisions (a)(2) and (d), to Regulation 4605's reference note. Board staff also recommended deleting the reference to BPC section 22978.7 from Regulation 4605's reference note because that section does not apply to manufacturers and importers and is not being interpreted, implemented, or made specific by the regulation, and moving the references to BPC sections 22979.4 and 22979.6, subdivision (c), in Regulation 4605's reference note so that all of the statutory references in the reference note are in numerical order.

Therefore, during the June 26, 2012, Business Taxes Committee meeting, the Board also unanimously voted to propose all of these additional amendments to the references to the BPC in Regulations 4603 through 4605 because the Board determined that the amendments were reasonably necessary to ensure that each regulation accurately cross-references the applicable revocation statutes and each regulation's reference note only refers to statutes that are being implemented, interpreted, or made specific by such regulation. The Board also determined that the additional amendments to Regulations 4603 through 4605 are necessary to address the confusion created by the regulations' current statutory references, and the Board anticipates that the Board and regulated persons will benefit from the additional clarity provided by the proposed amendments.

Finally, at the conclusion of the Board's June 26, 2012, Business Taxes Committee meeting, the Board voted to postpone proposing the amendments to Regulations 4601, 4603, 4604, and 4605 described above while the Board considered whether to propose the adoption of an additional regulation to implement, interpret, and make specific other

provisions of the Act. However, during the Board's January 15, 2013, Business Taxes Committee meeting, the Board unanimously voted to begin the formal rulemaking process to propose the amendments to Regulations 4601, 4603, 4604, and 4605 described above, and the Board did not decide to propose to adopt a new regulation at that time.

The proposed amendments to Regulations 4601, 4603, 4604, and 4605 were not mandated by federal law or regulations. There is no previously adopted or amended federal regulation that is identical to Regulations 4601, 4603, 4604, and 4605.

#### DOCUMENTS RELIED UPON

The Board relied upon Formal Issue Paper 12-007, the exhibit to the issue paper, and the comments made during the Board's discussion of the issue paper during its June 26, 2012, Business Taxes Committee meeting in deciding to propose the amendments to Regulations 4601, 4603, 4604, and 4605 described above.

#### ALTERNATIVES CONSIDERED

The Board considered whether to begin the formal rulemaking process to adopt the proposed amendments to Regulations 4601, 4603, 4604, and 4605 at this time or, alternatively, whether to take no action at this time. The Board decided to begin the formal rulemaking process to adopt the proposed amendments at this time because the Board determined that the proposed amendments are reasonably necessary for the reasons set forth above.

The Board also considered whether to amend Regulations 4603 through 4605 to provide for the reduction of a suspension within a range of between 1 and 20 days or to provide for the reduction of a suspension to "5 days," in addition to 0 days, 10 days, and 20 days. The Board decided that the latter alternative was more appropriate based upon staff's belief that a 5-day suspension period is long enough to deter violations of the Act, in some circumstances, and that Board staff has a sufficient amount of time to perform an inspection during a 5-day suspension period. The Board rejected the former alternative based upon the concern that shorter suspension periods, such as 1 day, might not be sufficient to deter violations of the Act and would be difficult for the Board to enforce. The Board did not reject any other reasonable alternatives to the proposed amendments.

There was no information presented to the Board to indicate that the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will have any adverse impact on small business. Also, no reasonable alternatives have been identified and brought to the Board's attention that would be less burdensome and equally effective in achieving the purposes of the proposed amendments or that would lessen any adverse impact the proposed amendments may have on small business. Therefore, the Board did not reject any alternatives to the proposed amendments that would be less burdensome and equally effective in achieving the purposes of the proposed amendments or that would lessen any adverse impact the proposed amendments may have on small business.

INFORMATION REQUIRED BY GOVERNMENT CODE SECTION 11346.2,  
SUBDIVISION (b)(6) AND ECONOMIC IMPACT ANALYSIS REQUIRED BY  
GOVERNMENT CODE SECTION 11346.3, SUBDIVISION (b)

The proposed amendments to Regulation 4601 simply require notices issued under the Act to be served in the manner provided by BPC section 22971.5 for the service of notices under the Act. As such, the amendments merely make the regulation consistent with the applicable statute regarding the service of such notices.

The Board already has discretion to reduce a suspension period to 0 days, 10 days, or 20 days when mitigating factors are present. The proposed amendments to Regulations 4603 through 4605 will also permit the Board to reduce a suspension period to 5 days when mitigating factors are present. The Board intends to use the 5-day suspension period in those situations where the Board would currently impose a 10-day suspension, but the Board determines that a 10-day suspension would be too harsh, and the Board does not intend to use the 5-day suspension period where the Board would currently reduce a suspension period to 0 days. Therefore, the Board anticipates that some persons will benefit from the proposed amendments by having their suspensions reduced to 5 days instead of 10 days.

Therefore, the Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses nor create or expand business in the State of California.

In addition, Regulations 4601, 4603, 4604, and 4605 do not regulate the health and welfare of California residents, worker safety, or the state's environment. Therefore, the Board has also determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not affect the health and welfare of California residents, worker safety, or the state's environment.

The forgoing information also provides the factual basis for the Board's initial determination that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not have a significant adverse economic impact on business.

The proposed amendments may affect small business.